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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1946

No. 1156

VIRGINIA YOUNG STOTT, MAY YOUNG LUBBEN, AND ELIZABETH JANSING,
Petitioners and Appellees Below,

vs.

TIDEWATER ASSOCIATED OIL CO. AND SEABOARD OIL CO. OF DELAWARE,
Respondents and Appellants Below

PETITION FOR WRIT OF CERTIORARI

To the Honorable the Chief Justice of the United States and the Associate Justices of the Supreme Court of the United States:

The petitioners, Virginia Young Stott, May Young Lubben, and Elizabeth Jansing, respectfully show to this Honorable Court:

A

Summary of the Matter Involved

This is a suit brought in the District Court of the United States for the Eastern District of Texas, by Virginia Young Stott, May Young Lubben, and Elizabeth Jansing,

petitioners herein, against Tidewater Associated Oil Company and Seaboard Oil Company of Delaware, respondents herein, for damage to their lands as a result of respondents' recycling operations. The trial was by the Court without a jury, and judgment was rendered in favor of petitioners against respondents for $7,798.94. An appeal from such judgment was taken by respondents to the Circuit Court of Appeals for the Fifth Circuit, which reversed the judgment of the District Court.

"Recycling" as used herein denotes an operation by which "wet" gas, withdrawn from the gas sands at withdrawal wells, is processed at a plant for liquid hydrocarbons known as condensate or distillate and resulting "dry" gas is forced by compressors back into the gas sands at injection wells (R. 63). The "dry" gas moves from the injection wells to the withdrawal wells (R. 64).

At the time recycling operations were begun, respondents, as original lessees, had held and operated an ordinary oil and gas lease on petitioner Jansing's lease since 1935 (R. 437). As assignees, they had operated an ordinary oil and gas lease on the lands of petitioners Stott and Lubben since 1933 except as to portions assigned in 1939 to Haynes B. Ownby Drilling Company (R. 306-12).

In making the assignment to Ownby, respondents did not assign their "entire" estate in the portion of the Stott and Lubben leases assigned, but "reserved and excepted" a one-sixteenth overriding royalty interest in the leases and in addition provided for extensive controls and rights of use and possession in the assigned premises including the right to control the use or sale of gas for the manufacture or extraction of gasoline and other liquid hydrocarbons.

The respondents, except for a 5-acre tract on the north and a small tract lying partly along the south, owned all

the leases adjoining petitioners lands on the north, east and south (F. of F. 11, R. 38).

Before respondents began their recycling operations, distillate was being produced on petitioners lands by separators located on each lease. On this distillate, respondents paid the usual one-eighth royalty provided for in the leases (R. 89 and 461).

Also, before respondents began their recycling operations, the parties were unable to reach an agreement on the unitization of petitioners' lands for the production of wet gas and recycling operations. Although the parties continued in their negotiations in good faith, they were never able to reach an agreement (F. of F. 12, R. 39).

Respondents began recycling operations in December, 1939, and continuously produced distillate up to the time of the trial (F. of F. 10, R. 38).

Their recycling operations ruined a portion of these lands for production of distillate by replacing the wet gas underlying them at the beginning of recycling with dry gas (F. of F. 18 and 20, R. 40-42).

Damages were awarded petitioners on the basis of one-eighth the value of the distillate which would have been produced on petitioners' lands by the separator method—*i. e.* ordinary lease operations (F. of F. 20, R. 40-42).

The District Court reached the following conclusions of law:

1

> "The defendants are liable because of the breach of their implied covenants not to injure the leases of the plaintiffs. They have done this by replacing the wet gas under a part of the plaintiffs' lands with dry or residue gas which had been processed in defendants' recycling plant. The processed gas had been reinjected into the gas holding formations through the reinjection wells in such a way as to move toward the plaintiffs' wells.

2

The defendants are liable as to the leases assigned by them to Ownby, by reason of the overriding royalty retained under the assignments, and by reason of the express provisions in the assignments giving them control over the disposition of the gas or condensate produced from the assigned acreage.

3

The plaintiffs should recover damages from the defendants resulting from the recycling operations of the defendants, as shown in the schedule set out in the Findings of Fact.

4

Unitization of plaintiffs' oil and gas leases is not authorized by the leases'' (R. 44-45).

On appeal, the Circuit Court of Appeals, contrary to the view of the trial court, found that there was no breach by respondents of any implied covenant not to injure petitioners' lands, and therefore did not consider whether the liability, if any, would extend to the bases assigned to Ownby.

B

Statement of the Basis for Jurisdiction

(a) The Supreme Court has jurisdiction to review the judgment here in question under Rule 38 and Section 240(a) of the Judicial Code as amended by the Act of February 13, 1925 (28 U. S. C. A., Sec. 347(a)).

(b) The date of the judgment of the United States Circuit Court of Appeals for the Fifth Circuit is December 30, 1946 (R. 537).

(c) The nature of the case and the rulings below are such as to bring the case within the jurisdictional provisions relied on, for the reasons set out herein for the allowance of the writ.

C

Questions Presented

This petition presents the following important question that should be settled by this Court:

1. Where the parties in good faith fail to reach an agreement for unitization and the lessees by recycling operations replaces the wet gas under the lessor's land with dry gas, has there been a breach of an implied covenant not to injure the lessor's lands?

D

Reasons Relied on for Allowance of the Writ

The Circuit Court of Appeals has decided an important question of local law in a way probably in conflict with applicable local decisions.

(1) The Supreme Court of Texas, in line with the long development of implied covenants in oil and gas leases, would probably hold that there is an implied covenant not to injure the lessor's land which would be breached by operations such as those of respondents in this case.

(2) The Circuit Court of Appeals for the Fifth Circuit has previously made this statement, in *Humphreys Oil Company* v. *Tatum*, 26 F. (2d) 882, certiorari denied 278 U. S. 633:

> "• • • The case here presented is much stronger in favor of petitioners than if the draining wells had been drilled by third persons. There would certainly

> be an implied covenant that the lessee would do nothing to impair the value of the lease of the lessor. If respondents saw fit to drill on their own adjoining land, it was their duty to use reasonable care in good faith to protect petitioners from damage caused thereby."

That statement represents the probable law in Texas, and the present holding of the Circuit Court of Appeals is in conflict therewith.

(3) The question at issue here is one of great importance to the vast Texas oil and gas industry. The recycling process is a relatively new method of operation in the Texas fields, and clear establishment of the applicable legal principles is necessary to guide the future course of such operations.

(4) The effect of the decision of the Circuit Court of Appeals in this case is virtually to establish compulsory unitization in Texas by judicial pronouncement. If such compulsory unitization is desirable, it is the function of the legislature to provide for it by statute, as has been done in a few states, rather than for the courts to impose it by their decisions.

WHEREFORE, your petitioners pray that a writ of certiorari issue under the seal of this Court directed to the United States Circuit Court of Appeals for the Fifth Circuit, commanding that Court to certify and send to this Court a full and complete transcript of the record and all proceedings in the case numbered and entitled on its docket, No. 11,669, Tidewater Associated Oil Company and Seaboard Oil Company of Delaware, Appellants, *v.* Virginia Young Stott, May Young Lubben and Elizabeth Jansing, Appellees, to the end that this cause may be reviewed and determined by this Court as provided for by the statutes of the United

States; and that the judgment herein of said Circuit Court of Appeals be reversed by this Court, and for such further relief as to this Court may seem proper.

Dated March 14, 1947.

VIRGINIA YOUNG STOTT,
MAY YOUNG LUBBEN, and
ELIZABETH JANSING,
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VS.

TIDEWATER ASSOCIATED OIL CO., AND SEABOARD OIL CO., OF DELAWARE, *Respondents*

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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I.

THE OPINION OF THE COURT BELOW

Opinion of the Circuit Court of Appeals for the Fifth Circuit was rendered December 30, 1946. It is shown at the end of the printed record.

II.

JURISDICTION

A complete statement of the basis of the jurisdiction of this court has been given under the heading B in the Petition for Writ of Certiorari. In the interest of brevity, it is not repeated here.

III.

STATEMENT OF THE CASE

A full statement of the case has been given under heading A in the Petition for Writ of Certiorari. In the interest of brevity it is not repeated here.

IV.

SPECIFICATIONS OF ERRORS

The Circuit Court of Appeals for the Fifth Circuit erred in reversing the holding of the District Court that the respondents (lessees here) by their recycling operations had breached their implied covenant not to injure the leases of the petitioners (lessors here) and for which injury they should respond in damages.

V.

SUMMARY OF ARGUMENT

POINT A

The Supreme Court of Texas, in line with the long development of implied covenants in oil and gas leases, would probably hold that there is an implied covenant not to injure lessors' lands which would be breached by operations such as those of respondents in this case.

As has been said by Professor A. W. Walker, Jr., one of the leading authorities in Texas on oil and gas questions, in his work "*The Nature of the Property Interests Created by an Oil and Gas Lease in Texas*" appearing in the Texas Law Review Vol. 11, Page 404:

> "The Courts seem to take the position that the agreement to pay royalty the amount of which depends upon the amount of production is sufficient to justify the implication of *any reasonable obligation* looking to the *protection* of the royalty." (Italics ours)

To the same effect is *Summers Oil and Gas*, Permanent Edition, Vol. 2, Paragraph 395, at Pages 301-309, inclusive.

See also

W. T. Waggoner Estate vs. Segler Oil Company, Com. App. 1926, 284 S. W. 921;

Cheek vs. Metzer, Comm. App. 1927, 291 S. W. 860.

The various covenants which have been implied in oil

and gas leases in Texas did not emerge full grown and at one time, as did Minerva, but have reached their present state as the result of the gradual growth of the law of oil and gas in Texas. It is inconceivable that the law of oil and gas has crystallized and become static—petitions' thought is that the law is alive, is dynamic, and is still growing.

In the situation here presented, the lessees' right to royalty can be protected only by an implied covenant on the part of the lessees not to carry on their recycling operations so as to injure lessors' lands. Let us now demonstrate this.

As has been stated in the Texas cases above, the compelling reason for the lessors to have made leases on the land in question was their expectation of royalty which is protected by recognized implied covenants in the *ordinary* operations of an oil and gas lease. In this case, no fault can be found with the *ordinary* operations of the leases in question.

But the lessees by *their* recycling operations *did* damage and injure the lessors' lands. The ordinary lease operations would not and did not prevent the encroachment of dry gas, a result of lessees' recycling operations.

Except by resorting to the Courts, the lessors had no way to protect themselves from lessees' recycling operations.

The lessors had no freedom to contract. They were bound by their leases to lessees. Those leases permitted only

ordinary lease operations—not recycling at one-half the royalty provided for in the lease contracts. (R. 428-440.) The lessors could not bargain with third persons for better terms than those offered by lessees because lessees at no time offered to surrender their leases. Lessors could not join with other persons for a recycling project of their own. And it must be remembered that the Trinity Company had carried on a successful recycling operation on a unit of 366 acres for a period of years. (R. 159 and 165.) Also, that lessors had 200 of the 366 acres necessary to duplicate this Trinity recycling operation. Securing an agreement for recycling on 166 additional acres should not have been difficult.

Thus, it appears to the lessors, that the only way their contractual interests could be protected would be for the Courts to declare the existence of an implied covenant on the part of the lessees that they not destroy their ability to produce wet gas and thus their ability in part to pay the royalty expected and provided for in the leases in question.

Here, the operations have already damaged a portion of this land and in order to make lessors whole for past injury, damages must be awarded them.

However, the lessees contend there is no implied covenant and further that they have offered fair and proper unitization. The Circuit Court's opinion is to the same effect. The lessors — petitioners herein — respectfully urge that

this decision is clearly erroneous. It would legalize unjust unitization because the unitization offers made to lessors did not fulfill the "purpose of unitization,"—as shown by the facts in the accompanying map, together with Judge Lee's own definition of this "purpose:" "to equalize the right of those royalty owners nearest the injection well and those nearest the producing well" (Opinion P. 7, lines 37-39). (This was also pointed out in Appellees Brief, P. 27, last paragraph and P. 29.)

And yet Judge Lee concluded: "there is no evidence to show that the prevailing plan (i. e. of unitization) was unfair." (P. 6, lines 23-26.)

The latter conflicts with the former and hence is erroneous.

The accompanying map attached to the last page of this brief shows the whole area operated by lessees' recycling plant,—the red crosses marking the producing wells, and the corners of the red triangle marking the injection wells. Other companies' injection wells are shown by *arrows*.

The black-bordered area (A-A) shows the largest unit into which appellees were ever to be incorporated—about 847 acres: it is situated next to or between the injection wells.

The red-bordered area (B)—about 1402 acres—is recycled area from which lessors were to be excluded, and much of it is the fartherest area from the injection wells.

Lessors' participation in the operation was to be terminated when the dry gas filled the A-A area, thus depriving them of a portion of their rights. Furthermore, this would legalize an unjustifiable unitization plan.

These maps, well locations, and acreage figures are from lessees—Defendant's Exhibits:

No. F—1½—(R. 416-417)

No. A—(R. 475-487)

No. H—(Vol. of Photostats and R. 157)

POINT B

The opinion of the Circuit Court of Appeals, Fifth Circuit, in Humphreys Oil Company vs. Tatum more correctly expresses the probable law in Texas on the question involved than does the opinion of the Circuit Court in the case at bar.

The Circuit Court of Appeals for the Fifth Circuit has previously made this statement, in Humphreys Oil Company vs. Tatum, 26 F. (2d) 882, certiorari denied 278 U. S. 633:

> "* * * The case here presented is much stronger in favor of petitioners than if the draining wells had been drilled by third persons. There would certainly be an implied covenant that the lessee would do nothing to impair the value of the lease of the lessor. If respondents saw fit to drill on their own adjoining

> land, it was their duty to use reasonable care in good faith to protect petitioners from damage caused thereby."

That statement represents the probable law in Texas, and the present holding of the Circuit Court of Appeals is in conflict therewith.

POINT C

The question at issue is one of great importance to the vast Texas oil and gas industry.

Recycling is a new method of production of petroleum products. The law of oil and gas as it existed in Texas has not kept up with this technological development. In order that the land owners and the oil producers may know how to conduct themselves in situations such as the one at bar, it is necessary that a final rule of conduct be outlined by this Honorable Court.

The gas of Texas is rapidly approaching in importance the greatness of its oil production. It is frequently predicted within the petroleum industry that a large portion of the future greatness of Texas depends upon its gas. Texas gas now is piped to many of the nation's industrial centers. The "Big Inch" pipeline deal recently completed is to take Texas gas to the East. A pipe line being built from El Paso to the Pacific Coast is to supplement the rapidly deminishing supply of gas in that area.

A large portion of the gas to be used both within and out of Texas will be processed through recycling plants. Such processing as will be done has to be done under pooling or unitization agreements voluntarily and freely entered into by the lessors and lessees, except where a lease is large enough to support an injection and withdrawal well itself. Where the parties—lessor and lessee—are unable to agree on a pooling or unitization plant, a rule of conduct in order to protect the contractual rights of the parties is needed.

Wide interest is centered on this case. Independent oil operators, major oil companies, attorneys, law professors, field and lease men in the oil business, all have expressed interest and concern. The case was a subject of comment in a recent address by Professor Walker, and it has been reported in the State Bar Journal. Interest is manifest; it is real and it is current.

The issue is one of great importance to the vast oil and gas industry of Texas.

POINT D

The effect of the decision of the Circuit Court of Appeals in this case is virtually to establish compulsory unitization in Texas by judicial pronouncement.

Denial of recovery to the lessors in the situation of the instant case denies to them any bargaining power whatever as to unitization. They must accept whatever terms

the lessee may offer, or suffer the loss of the wet gas under their land without recompense. Because of the existing lease, they cannot contract for unitization with any third parties. The only choice left to them is no choice at all.

It may be that unitization is scientifically and economically desirable, and should be compulsory. But this is a matter of policy, for legislative determination. Louisiana has, by statute, adopted pooling provisions (Louisiana Conservation Act, Act 225 of 1936), as has New Mexico (New Mexico Conservation Act, New Mexico Laws of 1935, C. 72). The Texas Legislature, however, has not seen fit to provide for compulsory unitization.

The situation might also be provided for in the terms of the original lease. Some oil and gas leases do contain a pooling clause granting the lessee the right to pool or unitize the leased land, under proper conditions. (See "Some Legal Problems Presented by the Pooling Provisions of the Modern Oil and Gas Leases", Shank, 23 Tex. Law Rev. 150). Petitioners' leases, however, do not authorize unitization. (R. 45).

Where statutes provide for compulsory unitization, they also provide safeguards to insure equitable treatment of each party. Likewise, lease provisions will authorize unitization only upon such terms as were considered fair and just by both lessor and lessee when negotiating the original lease. But compulsory unitization brought about

by judicial decree, as in this case, is entirely one-sided, allowing the lessee to determine whatever terms may suit him, with no statutory safeguards, and with no bargaining power left to the lessor.

WHEREFORE, it is respectfully submitted that the petition for writ of certiorari be granted.

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